Interlude: Panic! 1819

"Let every Shylock leave his hole, and in the open day boldly sharpen his knife, to take 'the pound of flesh' nearest the heart of his honest neighbor!" So wrote Baltimore journalist Hezekiah Niles about news from the Bank of the United States, in August 1818, that free exchange of notes among various regional branches would be suspended. Ranting wildly in graphic prose, Niles condemned the "Rag Barons" and their "paper system" for the "criminal" abuse of honest persons and taxpayers. Whatever suspicions he had harbored since 1816 about the wisdom of chartering a new national bank stood vindicated now that the crooks and swindlers in charge of this engine of currency manipulation had turned their "knives" upon the people, not just "skinning as heretofore" but cutting deep at the "arteries of the public body" to get "blood enough at once to swim in." So began the national nightmare known to history as the Panic of 1819.

Part and parcel of the postwar economic boom had been a dramatic expansion of the American money supply. As exports recovered from the wartime disruption, productivity expanded, and the promise of rapid growth returned, state and local banks, especially in the West and South, multiplied their loans and note issues with little regard for specie reserves or underlying values. All banks had stopped converting paper money into coin during the late war, so there was no effective check on this proliferation of banknotes. The newly chartered Second

1 Niles' Weekly Register, 5 Sept. 1818, 25. Emphasis in the original.
Bank of the United States was expected to bring about specie resumption in early 1817, but nobody had the legal authority to compel it. As a result, the new central bank joined the expansionists’ parade, showering loans and notes on eager customers until its total liabilities outran the specie in its vaults by a factor of ten to one! By early 1818, confidence in American banknotes began to slide. Spanish silver dollars commanded a 4 percent premium in Boston, creating the absurd possibility of drawing specie from the banks at par and selling it back for a profit — over and over again. “Good money” drained away to speculators and reckless western banks while questionable paper piled up in the hands of more conservative banks and in accounts owed (but not paid) to the treasury or the Second Bank.

In the summer of 1818, as this unstable monetary whirlwind spun out of control, the Bank of the United States suddenly called for a drastic contraction of credit. In the circular of August 23 (to which Niles was responding in the previous quotation), the bank stopped the flow of coin from solid to shiftless branches. At the same time, the directors called in millions in loans and demanded payment of outstanding balances owed by the state and local banks. Debtors and debtor banks scrambled for cash, calling in their loans and liquidating everything they could, driving down prices for the cotton, foodstuffs, and western lands against which such loans had been taken. In just over one year, the total demand liabilities (funds on deposit plus banknotes in circulation) of the Second Bank shrank from $23 million to $70 million. As the credit crunch rippled throughout the immature American banking system, business crashed to a halt and tens of thousands of individuals watched in horror as the value drained from their assets like water through a sieve. Technically, the monetary correction may have been a good thing, considering the dangerous inflationary pressures of the day, but the Bank’s draconian contraction set off a full-blown financial crisis the likes of which Americans had never seen before. As William Gouge put it in his sharply critical *Short History of Paper Money and Banking in the United States* (1833), “The bank was saved, but the people were ruined.”

There can be little doubt that the sharp contraction of the money supply is what triggered a downward spiral in American prices and employment. In 1816, there had been $68 million in banknotes in circulation; by January 1820, that number had dropped to about $45 million.3 The sudden removal of so much currency at a time when everybody needed cash to repay their debts unavoidably drove down the price of everything. Town lots, in which speculation had been especially heated, fell quickly by 50, 60, even 80 percent. Missouri Senator Thomas Hart Benton complained that the cities of the West were mortgaged to the Bank of the United States: “They are in the jaws of the monster! A lump of butter in the mouth of a dog! One gulp, one swallow, and all is gone.”4 Export staples such as cotton, flour, and tobacco lost just over half their value between August 1818 and June 1819 — although the physical volume of exports did not decrease. Public land sales crashed from $13.6 million in 1818 to under $2 million two years later.5 Thousands of individuals defaulted on their obligations to the federal land office. Falling agricultural prices made it impossible for farmers to repay their loans for capital improvements, exposing their means of a living to the danger of foreclosure. For want of cash, consumers stopped shopping and country merchants failed, awash in debt for expensive goods they could not even except. Country people retreated into the semi-subsistence ways of their fathers, making do with homemade things and what they could gain from local barter and exchange.

Town people faced new forms of distress rendered disastrous by the sharp rise in the concentration of propertyless workers. Unemployment spiked in 1819 and remained high for at least two years after that. One 1820 report from Philadelphia estimated employment in major handicraft industries as down four-fifths from what had prevailed in 1815 — even before the big boom. Hezekiah Niles thought as many as fifty thousand people were out of work in Baltimore, Philadelphia, and New York. Textile manufacturers laid off thousands of

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workers whose families had no other means nor even anywhere to go once evicted from company housing. It might be possible to blame real estate speculators or ever overreaching farmers and planters for getting themselves into trouble, but what crime had these people committed? For the first time since Independence, on such a massive scale, Americans experienced widespread distress through involuntary unemployment—that is, those who would work could not find paying work to do. One young man in Poughkeepsie, New York, despairing of an honest living, stole a horse in order to spend eight years in the state prison. There, at least, he would have bed, board, and employment.  

What could explain this sudden disaster in a land of plenty? People blamed the banks, of course, but others saw the boom as a reckless spree by a youthful nation drunk on the promise of luxury. Mordecai Noah, editor of the Tammany newspaper, the New York National Advocate, likened the condition of the nation to an “overgrown and pampered youth, with a constitution unhurt and passions unrestrained, vaulting and bounding to ruin.” Writing even before the panic was upon them, Noah had warned that “the want of industry is the foundation of the evil.” Easy money and high living tempted all, and Noah saw the hand of Providence looming over the country. Lazy wives and frivolous daughters came in for especially brutal criticism for seducing their husbands and fathers into the paths of ignoble extravagance. Fifty-dollar plumb cakes and thousand-dollar shawls, for Noah, summed up the complete loss of sensible values that obtained in the years before the panic. He further condemned urban life, especially the temptations offered to wage-earning urban clerks—unmarried youths, cash in hand, lured by all manner of vices, and bereft of the influence of home and elders to keep to the straight and narrow.  

At the core of Noah’s critique were the old-fashioned values of the rural economy: frugality, economy, and self-reliance. He acknowledged that there had been shocks before in the local systems of credit and barter, but an honorable merchant always was left with the freedom to “prop up his tottering affairs to the best advantage of his honest creditors.” Modern banking and “currency brokers” (his term for the heartless enforcers of contracts who cared not who you were nor to whom you owed money) had loosed upon the people a species of predators without consciences. They turned the credit system into an evil snare. Go back to the ways of your fathers, Noah exhorted: “There are so many ways of earning a morsel of bread honestly, that want, arising from indolence should never be tolerated...it is by Providence ordained that man is to live by the ‘sweat of his brow.’”  

For Noah and many others, the solution to “hard times” lay in retreating into the values of the moral economy that had obtained in the late eighteenth century: Eschew debt, avoid luxurious indulgence, suppress vicious habits, and tend to your own, autonomous living. Semi subsistence agriculture perfectly matched this ethic, but semi subsistence agriculture produced little surplus and did not grow the national economy. It contributed not a farthing to the engines of capitalist expansion on which national prosperity depended. Philadelphia booster and political economist Mathew Carey struggled to deflect the conversation in a more forward-looking direction. The present distress, Carey argued in 1819, offered no stimulus to industry: “There can be no industry without a motive: and it appears to me there is a great danger that our people will soon limit their exertions to the raising of food for their families.”  

Although Noah might applaud such retrenchment, Carey recognized that the system of economic growth would collapse without the further elaboration of the interdependencies, specializations, and divisions of labor that made the capitalist system effective. Do not retreat to the country, Carey cried: There were too many people on the land already. What the country needed was a program of home manufactures and a system of policy that protected home markets from exploitation by foreign capitalists. Banking reform was appropriate, but high protective tariffs would do more to engender a balanced economy and raise an “American system” of policy—the same thing Henry Clay was pushing in Congress—the point of which was to harness economic growth to American national interests.

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7 [Mordecai Noah], Address of the Society of Tammany, or Columbian Order, to Its Absent Members and the Members of Its Several Branches (Cincinnati: Morgan, Lodge, 1819), 8.  
9 Noah, Address of... Tammany, 10; New York National Advocate, 3 Sept. 1819. Emphasis in the original.  
10 Quoted in Rezneck, Business Depressions, 35.
In the face of the crisis of 1819, local institutions for poor relief found themselves crushed beneath the sheer volume of genuine distress. Some states reacted with stay laws, suspending foreclosures and debt repayments on the grounds that prevailing low prices made forced liquidations tantamount to theft. Some people called for the destruction of all banks, others for a return to easy paper money. A congressional investigation into the workings of the Second Bank of the United States found the vaults stuffed not with specie, but with IOUs signed by directors who had loaned vast sums to themselves and their friends, ignoring what safeguards had been written into their charter. But some forty members of Congress held stock in the Second Bank, and none wished to see it punished appropriately. Congress did reform the land system, restructuring some landholders’ debts, lowering the minimum price to $1.25 per acre, and eliminating altogether the four-year credit system. From now on, buyers of public land would have to pay cash or find lenders in the private sector. Throughout the country, debates raged over the sanctity of contract on one hand (without which the modern economy would not flourish), and on the other the protection of innocent persons (a traditional responsibility of the sovereign authorities) from predatory swindlers and fast-talking cheats who seemed mysteriously immune from the terrible sword of financial correction.

Clearly the Republic stood at the threshold of a new era. Prosperity for all – the booming potential of a growth economy – lay down the road toward the modern capitalist system; security for all – the enjoyment of a modest “competence” without exposure to undue risks in global financial markets – lay back the other way. State and local governments fumbled the dilemma, while the federal government blithely ignored “hard times” until they went away of their own accord. Modern economists now have ways of explaining these cyclical failures of confidence, but almost nobody in 1819 understood the technical forces that had crushed the system of credit and so drastically undermined prices. That cotton could be worth 24 cents one day and 11 cents the next made no sense: Cotton was a tangible product whose properties and usefulness changed not a whit overnight. One price or the other must be dishonest – one puffed up by intoxicating speculation, or the other forcibly depressed by the actions of crooked dealers. Not a generation away from the mercantilism of old, most Americans either accepted the scoldings dished out by the likes of Mordecai Noah or angrily searched for the scoundrels who must have wrecked the markets and profited handsomely in doing so. The Panic of 1819 had been a “teachable moment” in the emergence of a market revolution in the United States, but few could decipher correctly the moral of the story.

Painful as it was, the Panic of 1819 did not quite dislodge the traditional frameworks of economic virtue and providential blessing with which early Americans interpreted their fluctuating fortunes. Careful students looking back catch glimpses of the modern phenomena that accompany the business cycle in mature financial systems, but no one on the ground in 1819 knew what to look for or how to understand these market forces that rose and fell of their own accord and seemed to obey the commands of no man. It still made more sense to view them (like the Biblical plagues of Egypt) as warnings from an angry God, or as proof of corrupt conspiracies, than to embrace them as natural and inevitable features of the new economic system. Therefore, by 1822, when prosperity returned on a more stable footing, a generation of American white men recovered their confidence that they could navigate new economic waters to their own eventual improvement.

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